

**COMMONWEALTH OF MASSACHUSETTS
DEPARTMENT OF TELECOMMUNICATIONS AND ENERGY**

Investigation by the Department of Telecommunications and Energy) on its own Motion into the Appropriate Regulatory Plan to succeed) Price Cap Regulation for Verizon New England, Inc. d/b/a Verizon) Massachusetts' intrastate retail telecommunications services in the) Commonwealth of Massachusetts)	D.T.E. 01-31 Phase II
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**COMMENTS OF THE ATTORNEY GENERAL
ON THE PROPOSED PROCEDURAL SCHEDULE**

I. INTRODUCTION

These comments address case scheduling, a procedural issue that may have major rate consequences for the residential customers of Verizon Massachusetts ("Verizon" or "Company"). On August 1, 2002, the Department of Telecommunications and Energy's ("Department") Hearing Officer issued a Memorandum proposing a Procedural Schedule in this matter and scheduling a procedural conference for August 22, 2002.¹ The Hearing Officer indicated that the proposed Procedural Schedule would form the basis of discussion at the procedural conference, and that if parties wished to file comments on the proposed schedule, they should do so by August 15, 2002. The Attorney General now files these comments on the Department's proposed procedural schedule pursuant to the Hearing Officer Memorandum.

¹ In the August 1, 2002 Hearing Officer Memorandum, the Department proposed a procedural schedule dividing its retail rate investigation into two tracks and creating a third phase. Track A will review Verizon's Phase I Order compliance filing for retail business services, and Track B will review appropriate regulatory frameworks and service quality plans proposed by Verizon and others for retail residential services. Department August 1, 2002, Memorandum, p. 1. The Attorney General's comments primarily concern only Track B, the appropriate rates for residential customers.

II. PROCEDURAL HISTORY

On February 27, 2001, the Department opened an investigation to review the appropriate plan to succeed price cap regulation for Verizon. On June 21, 2001, the Department bifurcated the investigation. *See Scoping Order*, 6/21/01. The Department stated that in Phase I it would examine whether there was sufficient competition to deregulate any of Verizon's regulated residential or business services. The Department stated that Phase II of the investigation was designed to consider which alternative regulation plan – including traditional cost-of-service, indexed price cap regulation, and any intervenor-proposed plans – is most appropriate for retail services that are not sufficiently competitive to merit removal of pricing constraints. *Scoping Order*, pp. 17-19.

The Department concluded in its May 8, 2002 Phase I Final Order that Verizon is a monopoly provider of residential retail services - there was no showing of sufficient competition. *Phase I Order*, p. 99. Therefore, this phase of the docket “will consist of an investigation into which form of regulation, be it a continuation of price cap, a restoration of rate-of-return regulation, or some alternative, is appropriate for the level of competition demonstrated by our investigation in Phase I.” *Scoping Order*, pp. 17-18. On June 5, 2002, Verizon made a “Compliance Filing” setting forth its Phase II Plan. On June 25, 2002, the Attorney General filed Comments on the proposed plan requesting, among other issues, a procedural schedule that would allow for discovery, pre-filed testimony, evidentiary hearings, and briefing. The Department has not yet fully and specifically responded to these comments.

III. VERIZON PROPOSES GENERAL INCREASES IN RATES, REQUIRING A FULL AND THOROUGH INVESTIGATION.

A. Verizon's Proposal For A General Increase In Rates Requires Review Of The Company's Revenue Requirement.

On June 5, 2002, Verizon filed a regulatory plan ("Verizon 2002 Plan") that included a request for authority to implement, without further regulatory review, a potentially infinite number of five percent annual increases to its Residential Basic Services. Verizon's 2002 Plan, p. 1. Each increase would affect the majority of the Company's customers and would constitute a "general increase" in rates. G.L. c. 159, §20. By statute, the Department must hold a public hearing and make an investigation as to the propriety of such proposed rate changes. *Id.* The statute also specifies that the Company has "the burden to show that such increase is necessary to obtain a reasonable compensation for the service rendered." *Id.* Verizon has not provided any evidence to support the necessity of any increase in residential rates, much less five percent annual increases that may extend for years into the future without further Department review.

On April 12, 2001, in its original filing in this case, Verizon proposed to:

- * cap basic dial-tone and local usage rates for three years (reductions permitted, increases prohibited);
- * be permitted flexibility to choose to reduce basic residential rates in specific areas of the state during the three-year cap at its discretion (after three years, any increase in the basic residential service cap would require Department approval);
- * eliminate Touch Tone service charges in Massachusetts on a revenue-neutral basis;
- * restrict the pricing of all other residential services (*i.e.*, non-basic residential services) by requiring revenue neutral filings; however, Verizon proposes that it have the discretion to raise or lower rates in specific geographic areas.

Phase I Final Order, p. 16. Verizon thus proposed to cap or reduce rates for residential customers, not to implement general rate increases.

In its 2002 Plan, Verizon now proposes that it receive the authority, without further Department review, to implement substantial general increases in rates for Residential Basic Services. Verizon proposes to:

- * Raise all Massachusetts residential customers' basic monthly rate for telephone services by between \$1.90 and \$2.37 per month (by increasing the monthly dial tone charge from the current \$9.91 to between \$11.81 and \$12.28). Residential rates purportedly would be raised to recover Verizon's claimed lost revenues (\$59 million annually) from changes in access fees it used to recover from interexchange carriers like AT&T, WorldCom, and Sprint. Also, Touch-Tone service (formerly optional) would be included in the dial tone rate.
- * Have authority to implement additional future rate increases for residential basic service not to exceed five percent per year without Department review, with the option of raising rates more than five percent annually with prior Departmental permission.
- * Eliminate or revise existing service quality standards for residential services set by the Department in D.P.U. 94-50.
- * Increase the credit for its 163,000 subsidized LifeLine customers equal to the increase in residential dial-tone rate.

The majority of Verizon's customers are residential. Residential services are the main category for which Verizon has not attempted to show "sufficient competition," and for which the Department will still regulate and set rates. *Phase I Order*, p. 99. Verizon's proposal for authority to implement rate increases of up to five percent per year, without further review by the Department, constitutes a request for more than one "general increase in rates" as that term is used in the statute. *See*, G.L. c. 159, §20.

The Department conducted its last general rate case review for the Company in 1986 and 1987, based on data that are now more than 15 years old. *New England Telephone and Telegraph Company*, D.P.U. 86-33 (1987). As the Department has recognized, telecommunications is an industry in which overall costs are declining. *See e.g., AT&T*, D.P.U. 91-79, p. 45 (1992). Accordingly, under the Department-approved Price Cap Plan which expired

August 15, 2001, business customers received \$296 million in rate reductions. Only last year, in this very case, Verizon filed a regulatory plan that capped residential dial tone and usage rates for three years (reductions permitted, increases prohibited) and allowed other residential services to change only on a revenue-neutral basis.

The Department may not properly rely on data from the 1980s to presume in 2002 that increased rates would be just and reasonable and that such increases are needed to yield reasonable compensation.² G.L. c. 159, §20. Before authorizing Verizon to implement any residential rate increases, the Department should order Verizon to file a full cost of service/revenue requirement and a fully allocated cost of service study so that it can properly investigate the need for any proposed increase.

The Department should amend the proposed schedule because it does not provide sufficient time for a general rate case investigation, including revenue requirements, affiliate transactions (G.L. c. 159, § 34A) and cost allocation issues. In addition, the Department should amend the schedule to reflect the statutory requirement that Verizon, not intervenors, bears the burden of proof for the proposed general rate increases in basic residential rates. G.L. c. 159, §20.

B. The Department Should Order Verizon To File A Fully Allocated Cost Of Service Study.

The Department should require Verizon to file cost of service studies to support the request for a annual residential rate increases of up to five percent. Verizon has the burden of

² The Department stated in its “tentative conclusions” that “historical evidence has shown that residential rates are likely below their efficient levels,” *citing* D.P.U. 89-300. D.T.E. 01-31-Phase I, pp. 96, 100, May 8, 2002.

proof to demonstrate that its proposed increases are not unjust, unreasonable, or improper rates, or allow excess revenues. G.L. c. 159, §§ 16, 20.³

The legislative framework in Chapter 159 requires that the Department assess Verizon's Plan to determine whether it provides adequate compensation for services rendered, and is not unjustly discriminatory, unduly preferential, or otherwise in violation of any law.⁴ G.L. c. 159, §§ 14 and 20. A fully allocated cost of service study is a necessary starting point to show whether any increases to residential services would be just and reasonable.

A review of the Company's current rates remains imperative in this case because the Price Cap Plan expired and twelve to fifteen years have passed since the last comprehensive review, rendering the underlying record evidence stale and therefore unreliable.

C. The Procedural Schedule Should Allow A Full Investigation Of This Proposed General Rate Increase.

The Department, therefore, should set the normal six month rate case schedule following proper filings by Verizon. G.L. c. 25, §18. Verizon should make complete revenue requirement filings, including affiliate transactions, and cost allocation-rate design filings two months after the procedural conference, on October 22, 2002. This proposed procedural schedule would then yield a Department order by April 22, 2003:

³ "At any such hearing involving any proposed increase in any rate, joint rate, fare, telephone rental, toll or charge, the burden of proof to show that such increase is necessary to obtain a reasonable compensation for the service rendered shall be upon the common carrier." G.L. c. 159, § 20. The Department's final procedural schedule, and statements regarding "tentative conclusions," must not shift any aspect of the burden of proof – either production or persuasion – from the Company to the intervenors.

⁴ "[F]rom the earliest cases, the end of public utility regulation has been recognized to be the protection of consumers from exorbitant rates." *Washington Gas Light Company v. Baker*, 188 F.2d 11, 15 (1950).

Track A: Compliance with Phase I Order Directives on Verizon Retail Business Services

August 22, 2002	Open discovery period begins
September 30, 2002	Discovery period closes
October 17, 2002	All responses must be filed with the Department
October 31, 2002	Parties petition Department for evidentiary hearings on Track A issues

Track B: Regulatory framework for retail residential services and proposed service quality plans

October 22, 2002	Verizon files direct testimony with cost of service studies. Intervenor open discovery period begins (10 business days for information responses, 5 calendar days for record responses)
December 10, 2002	Intervenors file any testimony, including alternative regulatory plans and alternative service quality plans
December 20, 2002	Information requests completed (all parties)
January 6, 2003	All responses must be filed with the Department and parties by this date.
January 14 through February 14, 2003	Evidentiary hearings
March 4, 2003	Intervenors' initial briefs due
March 18, 2003	Verizon initial brief due
March 25, 2003	Intervenors' reply briefs due
April 1, 2003	Verizon reply letter (if any) due
April 22, 2003	Department order issued

IV. THE DEPARTMENT SHOULD ORDER AN INDEPENDENT AUDIT

The Department should also order a complete audit of the Company's regulatory accounting by an independent, third party auditor approved by the Attorney General.⁵ Such an audit would assure the ratepaying public that rates are not yielding excess compensation to Verizon, and would help restore public confidence in light of recent disastrous accounting irregularities in the telecommunications industry. Ordering an independent audit is consistent with recent action by the California Public Utilities Commission for Verizon California. *See, Verizon California Incorporated*, Docket # R.01-09-001, I.01-09-002, August 6, 2002 (proposed

⁵ To maintain impartiality, the Company should pay the costs associated with the examination, but the Attorney General should retain the auditor to conduct the review.

order finding that Verizon California had understated its profits from 1996-2001 after a similar audit by the Office of Ratepayer Advocates).

V. CONCLUSION

The Attorney General urges the Department to amend the procedural schedule to assure a full and thorough investigation of the proposed rate increases for consumers.

Respectfully submitted
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